

Message Text

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ACTION NEA-10

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FM AMEMBASSY TEL AVIV
TO SECSTATE WASHDC 7925

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SUBJECT: TEL AVIV STOCK EXCHANGE ACTIVITY SOARS

1. IN VERY HEAVY TRADING, THE TEL AVIV STOCK EXCHANGE LAST WEEK SAW STOCK PRICES GYRATING WILDLY IN RECORD TURNOVER. BY TUESDAY, AUGUST 16, THE STOCK INDEX WAS ABOUT 80 PERCENT ABOVE EARLY 1977 LEVELS AND THE VALUE OF STOCK TURNOVER REACHED A RECORD OF IL 146 MILLION. DURING TUESDAY'S STOCK PRICE SURGE, 41 SECURITIES WERE "BUYERS ONLY." ON WEDNESDAY, PROFIT-TAKING SET IN AND STOCK FELL SHARPLY, WITH 76 SHARES MARKED "SELLERS ONLY" AND TURNOVER REACHING A VALUE OF IL 135 MILLION. NEVERTHELESS, BY THE END OF THE WEEK, THE STOCK AVERAGE WAS STILL 70 PERCENT ABOVE EARLY 1977 LEVELS.

2. SEVERAL FACTORS HAVE BEEN CITED AS CONTRIBUTING TO INCREASED STOCK MARKET ACTIVITY:

-- EXCESS LIQUIDITY IN THE ECONOMY FOLLOWING THE WAGE HIKES WON IN THE PRE-ELECTION PERIOD. ACCORDING TO THIS THEORY, WHICH IS ADVANCED BY GOI SOURCES, MANY WAGE EARNERS HAVE PUT MONEY INTO THE STOCK EXCHANGE WITH PART OF THEIR EXTRA DISCRETIONARY INCOME.

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-- THE IMPROVED OUTLOOK UNDER THE NEW GOVERNMENT FOR THE DEVELOPMENT OF THE STOCK EXCHANGE AS A MAJOR VEHICLE IN THE LOCAL CAPITAL MARKET. FINANCE MINISTER EHRLICH HAS NOTED IN RECENT INTERVIEWS THAT THE LIKUD FAVORS THE EXPANSION OF THE TEL AVIV EXCHANGE AS AN ALTERNATE SOURCE OF DOMESTIC INVESTMENT CAPITAL TO

ISRAELI FIRMS WHICH HAD HERETOFORE RELIED ON THE GOI AND LOCAL INVESTMENT BANKS FOR FUNDS. THESE STATEMENTS MAY HAVE GIVEN A BOOST TO CONFIDENCE IN THE FUTURE ROBUSTNESS OF THE MARKET.

-- A CHANGE IN EXPECTED RATES OF RETURN FOR EQUITIES AS OPPOSED TO OTHER FINANCIAL ASSETS. AFTER THREE MONTHS OF THE LIKUD GOVERNMENT, BUSINESSMEN AND THE INVESTING PUBLIC APPEAR TO EXPECT THAT THE PRIVATE SECTOR WILL BE ALLOWED TO GROW AND PROFIT UNDER FREE MARKET ORIENTED POLICIES AND THAT THE RATE OF INFLATION WILL DECLINE. THIS OUTLOOK LEADS TO A REEVALUATION OF THE IDEAL COMPOSITION OF AN ASSET PORTFOLIO. FUNDS HAVE MOVED INTO EQUITIES FROM FIXED INCOME SECURITIES AS INDEX-LINKED BONDS HAVE MOVED IN OPPOSITE DIRECTIONS FROM STOCKS. FOREIGN CURRENCY SPECULATION HAS ALSO DIED DOWN. THE NATAD INVESTMENT DOLLAR RATE FELL TO IL 11.46 ON AUGUST 19, BELOW IT UNOFFICIAL FLOOR OF A 15 PERCENT PREMIUM OVER THE MARKET RATE OF \$1 EQUALS IL 10.11. THE BLACK MARKET RATE IS EVEN LOWER AT \$1 EQUALS IL 11.00.

3. COMMENT: WHILE THE MOVEMENT AWAY FROM BONDS AND FOREIGN CURRENCY INTO STOCKS CAN BE EXPLAINED BY CHANGES IN RELATIVE RATES OF RETURN, THE FRANTIC MARKET ACTIVITY OF THE PAST TWO WEEKS APPEARS TO BE DUE IN UNCLASSIFIED

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PART TO A WAVE OF SPECULATIVE FEVER WHICH OVERCAME MANY ISRAELIS. PRICE-EARNINGS RATIOS OF MANY STOCKS HAVE REACHED LEVELS WHICH ARE RIDICULOUS IN ECONOMIC TERMS. GOI AND EXCHANGE OFFICIALS' WARNINGS TO THE PUBLIC WENT UNHEeded BY MANY AND A GREAT DEAL OF MONEY HAS CHANGED HANDS AS THE MARKET HAS GONE THROUGH WILD GYRATIONS. RUMOR HAS IT THAT MANY PEOPLE OF RELATIVELY MODEST MEANS HAVE TAKEN FLYERS. ALTHOUGH IT IS LIKELY THAT TRADING WILL QUIET DOWN BEFORE LONG, IT IS IMPORTANT THAT THE SPECULATIVE BUBBLE BE DEFLATED BY STAGES RATHER THAN POPPED IF THE ENHANCED POSITION OF THE MARKET AS A FINANCIAL INSTITUTION IS TO BE PERMANENT.
LEWIS

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